SD Publication Series
Office of Sustainable Development
Bureau for Africa

Endowments in Africa

A Discussion of Issues for Using Alternative Funding Mechanisms to Support Agricultural and Natural Resources Management Programs

Technical Paper No. 24
August 1996

USAID

This publication is part of the

Sustainable Financing Series

USAID / Africa Bureau
Office of Sustainable Development
Productive Sector Growth and Environment Division
Technology Development and Transfer Division

Activity: *Sustainable Financing*
Objective: *To assist African agricultural research and natural resources management institutions strengthen their financial base.*

The series includes the following publications:

- Sustainable Financing: *Background Paper*
- Endowments in Africa: *A Discussion of Issues for Using Alternative Funding Mechanisms to Support Agriculture and Natural Resources Management Programs*
- Basic Guide to Using Debt Conversions
- Commercialization of Research and Technology
- Checkoffs (Voluntary Levies): *New Approaches to Funding Research, Development and Conservation Programs*
- Sustainable Financing*: Framework, Concepts, and Applications*

For more information about the series, contact:

Publication / Dissemination Officer
USAID/AFR/SD/PSGE
(1111 N. 19th Street, Suite 307, Rosslyn)
Rm 2744 NS, Washington, D.C. 20523-0089
Fax: 703-235-5064

Productive Sector Growth and Environment Division
Office of Sustainable Development
Bureau for Africa
U.S. Agency for International Development

Endowments in Africa
A Discussion of Issues for Using Alternative Funding Mechanisms to Support Agricultural and Natural Resources Management Programs

August 1996

Disclaimer of Endorsement
The opinions and recommendations in this book represent the views of the author and do not reflect the views of either USAID or the University of Missouri. USAID's Bureau for Policy and Program Coordination and Office of General Counsel have issued guidelines for use by USAID missions in deciding whether and how to create an endowment. The guidelines can be obtained by writing to: USAID, Bureau for Policy and Program Coordination, Rm 3975 NS, Washington, D.C. 20523.

Publication services provided by **AMEX International, Inc.**
pursuant to the following USAID contract:

Project Title:	Policy, Analysis, Research, and Technical Support Project
Project Number:	698-0478
Contract Number:	AOT-0478-C-00-3168-00

USAID

Contents

Foreword

Two recent trends in development assistance have added urgency to the topic of this guide. The first is an increasing concern that the level of future flows of development aid will decrease. The second is the emphasis on "sustainable development."

Decreasing foreign aid flows mean that programs in critical sectors must look to new sources to assure adequate, future financial support. Donors and aid recipient institutions view endowments as providing two kinds of options to alternative funding: they are a way to "smooth" funding flows so as to match financial need over time; and the process of setting up and funding an endowment offers several opportunities to build partnerships among governmental agencies, nongovernmental organizations, and the for-profit private sector. This guide outlines how these partnerships can mutually benefit all partners.

Donors and developing countries are increasingly concerned about ways to make economic development more sustainable. Endowments contribute to this goal because they make key institutions whose programs are dedicated to long-term goals more financially stable. Such stability means that these institutions (e.g. environmental agencies and agricultural research organizations) can plan more strategically for long-term goals because they are more confident of their financial support.

Endowments make another indirect, yet major contribution to sustainable development. Setting up an endowment that has credibility within civil society requires a process that is transparent and highly participatory. Once that process yields a creditable, well-administered and well-governed endowed institution, civil society benefits by having a new center of influence that is a force for dialogue and consensus building. In short, an endowment stimulates growth in a pluralistic democracy because it creates strong and independent institutions dedicated to long-term societal benefits.

Since writing this guide, USAID's Africa Bureau (USAID/AFR) has commissioned three additional guides on alternative development financing: debt conversions; checkoffs (voluntary levies); and commercialization of research and technology. Taken together, these four guides represent a body of knowledge that enables developing country institutions to learn about possible options for financial innovation, how to design those options, and policy and regulatory reform required to make those options work. These guides are primary reference materials for all institutions.

This guide has been completed under the sustainable financing activity in USAID/AFR, through the Office of Sustainable Development, Productive Sector Growth and Environment Division (SD/PSGE). The activity assists African agricultural research and natural resources management institutions strengthen their financial base. The guide will be useful to African organizations and other donors considering or engaged in designing an endowment.

Phil Jones
Natural Resources Management Unit Leader
USAID/AFR/SD/PSGE

Preface

This guide had its origin in Madagascar, when the author, Paul Weatherly, as part of USAID's Knowledge, Education, Participation in Environmental Management (KEPEM) project design team, wrote a report on how to create an endowed foundation in Madagascar for the purpose of providing sustaining funding for natural resources conservation and management. Subsequently, Weatherly was contracted to write a set of guidelines for African institutions that were considering using endowments. His analysis included field visits and peer review. The latter resulted in a Washington, D.C. colloquium of 50 representatives from a broad cross section of organizations interested in foundations and endowments in Africa.

Another key step in preparing this guide was a "peer" review meeting on the campus of the University of Missouri in Columbia, Missouri. Participants at that meeting recommended several changes and additions, which, for the most part, have been incorporated in this guide. Besides the author, this guide is also the result of contributions from many individuals. Chief among them were Tony Pryor and Jeff Hill of USAID/AFR/SD/PSGE. Other contributors include the University of Missouri and Winrock International.

Executive Summary

Africa faces the prospect of less development aid in the post Cold War era. Already, donors are reducing their presence in many countries. This scale back brings to a crisis a problem that, though long recognized, has yet to be addressed: the sustainability of institutions and programs necessary to meet long-term goals and supply continual services.

Endowments offer an effective tool that donors and government can use to make these institutions and programs more self-sustaining. Not only do endowments insulate institutions and programs from inconstancy in governmental- and donor-funding levels, they also help achieve true maturity in institutional and program management. If managed successfully, endowments upgrade institutional capacity to create and manage programs that are more effective.

Using money for endowments effectively will require that "stakeholders"—those with an interest in the use of endowment income—participate in the process of endowment creation and in the management of endowed institutions. Endowed institutions will have to become more accountable to governmental agencies responsible for public sector programs. Donors have a role to play not only in funding seed endowments, but in helping work through the process of institutional change necessary to prepare for the increased independence and responsibility required to oversee and use an endowment.

While governmental and nongovernmental institutions supporting economic and social development in Africa face many challenges, they have been able to rely on continued, if somewhat variable, donor support since independence. However, with donor support declining, governments are more reluctant to provide support, especially in the sectors of agriculture and environment that traditionally lie at the core of the concept of "sustainable" development.

Well established agricultural research institutions are concerned that their gains of more than 30 years will be lost. Newly created environmental departments are concerned that their long-term programs, so carefully planned in post-UNCED National Environmental Action Plans (NEAPS), will never have a chance because long-term, stable sources of funding are not apparent.

In this climate of uncertainty, African countries and non-regional donors are searching for new ways to put funding sources into long-term partnerships with program-implementing institutions. Three institutions have committed themselves to support innovative financing: the Special Program for African Agricultural Research (SPAAR), an Africa-wide consortium of donors and national agricultural research systems with a corresponding secretariat; the Multi Donor Secretariat (MDS); and the Network for Environmental Sustainable Development (NESDA). Their commitment has taken the form of a joint initiative to help key African institutions achieve a qualitative and quantitative gain in financial stability.

Few African institutions have the management skills, either financial or program, to take on an endowment. Consequently the SPAAR/MDS/NESDA sustainable finance initiative places high emphasis on building such capacity in key African institutions.

Experience in a number of places—in Africa and elsewhere—points to the centrality of a capital endowment in order to achieve a gain in financial stability. This is not simply because an endowment is the only way to broaden funding bases and build supportive relations with new types of funding. Rather, having an endowment requires that an institution have the capacity to manage responsible financial resources. Because an endowment supplies indefinite income, the institution responsible needs a different and more sophisticated management ability. It needs to be able to manage its finances and oversee program expenditures independent of a donor-paid technical advisor or program auditor.

Although the process of building management capacity is a daunting task, it will bring rewards greater than the ability to simply manage an endowment. The process of acquiring these skills will make the institution more fit for conceiving and implementing other innovations that could help secure steadier funding, such as voluntary levies on producers, special user fees, royalties from commercialization of new technologies or crops, and partnerships with governments that allow creation of special tax districts for support of either agricultural or environmental programs.

The process of creating an endowment, in light of current donor regulations, will likely have two tracks: financial and institutional. The financial track (legal oversight, trust fund management, etc.) builds an arrangement that supplies steady income for an organization or group of organizations active in a particular sector. The institutional track (program management, expenditure accountability, etc.) builds an organization that can plan and use the income effectively over a number of years, with the long-term goals of a particular sector in mind. With organizational maturity, the two tracks will converge when the control of the endowment passes to the fully competent organization. Achieving this level of maturity is as important for sustainability as having steady income from an endowment.

The concept of endowments is rapidly moving into the forefront of development because it answers two needs that most development strategists agree are at the heart of the idea of what development is "sustainable." One is the need for a greater variety of funding sources that are indigenous and based on partnerships of mutual interest. The other is the need for institutions that can manage their affairs independent of traditional foreign aid donors.

Donors can help by providing a forum around which a group of actors—"stakeholders" that will play a role in either the financial innovation, upgrading or both—can coalesce. The importance of having such a coalition is to learn lessons from other efforts to develop endowments, both in Africa and elsewhere.

This handbook recommends a sequence of decisions and a sequence of steps to implement an endowment. It offers specific advice based on lessons learned in other countries. Underlying the advice is an appreciation of the fundamental issue of endowment design: *How to balance independence, necessary to allow an endowed institution to maintain a long-term vision, with controls that check a shift in purpose or slide toward corruption*. Donors of endowment funds can play a temporary oversight role, but ultimately the endowed institution and its partners needs to assume this responsibility.

Among these partners, governmental agencies and nongovernmental organizations (NGOs) should have an explicit, mutually acknowledged degree of control over an endowed institution. Typically, such control is exercised by having government and NGOs select representing board members. In some cases, these board members, together with a donor representative, have veto power over institutional decisions. However, such power, no matter how carefully defined, casts a cloud of uncertainly over an endowed institution. NGOs and their leaders may be reluctant to commit talents to an institution under such a shadow, but their commitment gives a mandate that is necessary for an endowed institution to operate.

Even with clever, creative built-in checks and balances and a mandate from the NGO community, a need for a supportive regulatory framework for overseeing the activities of endowments and endowed institutions remains. Since African countries, like other developing countries, historically have had few endowed institutions, there is little effective governmental regulation. Donors can play a key role by putting such regulatory reform on their agendas for policy loans and grants. They should support technical assistance to help develop appropriate regulations.

Besides long-term financing, fund raising offers crucial benefits for endowed institutions. Because donors only support institutions that have effective programs and avoid conflicts of interest, the development of an aggressive and innovative fund-raising program creates a powerful incentive for honest and effective management.

Increasingly, the local and international media are becoming crucial to successful fund raising. Stories of social and environmental problems generate interest and fund-raising contributions. However, the institution must have creditability in the public mind and press.

For different reasons, governments and NGOs tend to operate within given sets of rules. While both may seek to change the status quo, they usually do so in incremental fashion. An endowed institution is likely to be independent from either of these traditions and able to identify and precipitate more qualitative types of changes, such as opening new markets, building broad coalitions advocating fundamental policy changes, and promoting acceptance of new attitudes.

The growth of endowed institutions committed to agricultural research will help evolve traditions such as research priority setting from fixed approaches of 20 years ago. Soon it may be more likely that breakthroughs in productivity will come from highly innovative marketing and/or investment arrangements than from traditional crop varietal research.

Environmental institutions often tend to react adversely to the suggestion of cooperating with the private sector. However, these institutions can learn much about the mechanics of such cooperation from agricultural foundations that have pioneered the ability of using combinations of grants and investments to create new enterprises that eventually become investment-worthy businesses. The growth of endowed environmental institutions should inspire reluctant environmental institutions to consider mutually beneficial and environmentally responsible partnerships with the private sector. The incentive would come from having the opportunity to invest their endowed capital in private businesses.

Glossary of Acronyms and Abbreviations

AFR	Africa Bureau (USAID)
EPAT	Environmental Policy and Training Project (USAID / Global Bureau Project)
FHIA	Honduran Institute for Agriculture
FONAMA	Fund for Nature and the Environment (Bolivia)
FUNDAGRO	Fund for Agriculture (Ecuador)
GEF	Global Environment Facility
IUCN	International Union for the Conservation of Nature
KEPEM	Knowledge, Education, Participation in Environmental Management (USAID / Madagascar Project)
NEAP	National Environmental Action Plan
NGO	nongovernmental organization
PROFONANPE	Peruvian Fund for Nature
PSGE	Productive Sector Growth and Environment Division (USAID/AFR/SD)
PVO	private voluntary organization
SD	Office of Sustainable Development (USAID/AFR)
UNCED	United Nations Conference on Environment and Development
USAID	U.S. Agency for International Development
WWF	World Wildlife Fund

1. Case for Endowments

INTRODUCTION

This guide offers donors, governments, and leaders of civil society advice for considering the use of endowed funds to build local institutions. It contains three sections, each of which gives progressively more specific advice on establishing an endowment:

- *Section 1. Case for Endowments* will help decision-makers and political leaders by identifying reasons for endowments. It describes the role endowments can play in sustainable development by strengthening key local institutions. These stronger and more influential nonprofit institutions can, in turn, make civil society more robust, becoming more capable partners for the governmental and for-profit sectors.
- *Section 2. Alternatives to Endowments and Foundations in Africa* provides advice for those who will be responsible for creating an endowment. It takes a look at endowment design alternatives and offers a conceptual framework for thinking about an endowment's strategic relevance, and its vital and complex roles in a civil society.
- *Section 3. Steps to Starting an Endowed Foundation* gives practical advice and resources on creating an endowment. It is useful to donor and foundation organizers, directors, and constituency groups.

The Sustainable Financing Initiative

This guide is the first in the "Sustainable Financing Initiative," a series of studies managed by the University of Missouri at Columbia. The Initiative has four goals:

- identifying and promoting innovative financing tools as a way to strengthen institutions (with a first priority on agricultural research and natural resources management);
- advancing theory and practice of creating endowed institutions, as well as strengthening existing institutions as a strategy to address long-term needs;
- linking unfolding experience among African countries and between Africa and other regions, especially Latin America; and
- designing and disseminating products—handbooks, papers, training—to a broad audience.

In addition, the Initiative plans to issue three more guides on other innovative financing techniques:

- checkoff programs (useful in supporting agricultural research);
- commercialization; and
- "debt for development" swaps.

As interest develops, the Initiative will produce and distribute additional guides and papers that address specific topics.

Purpose and Scope

Purpose: Provides guidance on how endowments in Africa foster and support sustainable development activities. It gives a conceptual framework for understanding and choosing among alternative "creation paths" of an endowed fund, whether the fund is established with an existing institution or a new foundation is created.

Scope: Traces the steps of creating an endowment. It answers five key questions:

- What is the purpose of an endowment?
- How is endowment revenue used?
- Who has oversight on assets and grants?

- How are funds moved to an endowment?
- What process creates an endowment?

Beyond process and scope, this guide offers recommendations on designing key areas of an endowment, such as its governing and management structure, relationship to the community, and public sector activities, investment programs, and duration.

The aim here is to offer practical and relevant advice for the entire spectrum of endowment development. The issues considered range from budget support for an existing institution to the creation of a new institution dedicated to operating as a grant-making foundation. The sectors examined cover a rich variety of development activities. However, since there is a greater need in the fields of agricultural research and environment, we will emphasize these sectors.

While this guide provides advice useful to recognizing and managing general risks, each situation will have its own unique opportunities and constraints. Endowment creators should allocate sufficient time and funds to the exploratory and design phases, allowing for full exploration of the challenges encountered along the path to success.

WHAT IS THE PURPOSE OF AN ENDOWMENT?

Endowments are an effective mechanism for accomplishing certain types of development tasks. They can be used to strengthen institutions that have critical roles in high priority sectors—agriculture, health, and the environment—by making these institutions more financially and managerially independent. Endowments can also empower constituencies whose day-to-day activities are essential to the success of a long-term sectoral strategies. They can also assist with decision-making.

Endowments provide those who hold a stake in a sector—“stakeholders”—a means of participating in decisions and management. They also allow donors to strengthen local institutions that sustain a participatory dialogue on sectoral priorities and programs. As such, endowments can serve as a cornerstone of sustainable development.

Why an endowment? A primary reason for donors to consider an endowment stems from a need to provide a long-term source for financing responsible elements within society, to help them build commitment to the solution of development problems. Achieving this purpose, the long-term commitment to “sustainable development” goals, requires that various communities, both local and national, participate in shaping endowment-funded programs.

Solutions to economic development issues demand responsible trade-offs between conflicting, but legitimate desires. Often these conflicts are rooted in antagonisms between different groups within a society.

No foreign donor or international nongovernmental (NGO) has the moral authority of an indigenous institution in playing an on-going role in resolving these differences. It is more effective for differences to be solved through local initiatives that include different viewpoints while balancing present aspirations and future needs. Donors can support this process by building capacity in local institutions.

An endowment must marshal local political and financial support to have a policy role at any national level. Donors can support the development of this kind of legitimacy with financial, technical, and morale support. They strengthen an endowment's efforts to preserve as appropriate, protect where necessary, and develop when possible, a nation’s natural, human, and social resources. Whether preserving biological diversity, cleaning up water resources, or setting research priorities, the endowed institution needs financing that is secure in the face of changes in national policy, political power, or donor priority.

Acknowledging Society's Responsibility. If donors want to see environmental viewpoints flourish, their best strategy would be to acknowledge that ultimate responsibility rests within the society. Environmental problems can be addressed through the involvement of a broad cross-section of society that participates in setting local and national priorities and responses. In this case, a donor's most sustainable intervention would be to plant environmentalism at the grassroots level and nurture its growth.

In Latin America, there are many examples of well-regarded uses of endowment mechanisms, some with donor support and some independently operated: Fundación Chile (Chile); Fundagro (Ecuador); FHIA (Honduras); and PROFONANPE (Peru). Where institutions were once missing altogether, Latin American donors have created new endowed institution that bring together critical masses of talent and leadership.

How Governments View Endowments

As donor aid for development activities continues to shrink, the ability of public and nonprofit private sector institutions to meet sustainable long-term development goals becomes a key issue. Endowments that build the capital base of strategic institutions present an alternative approach for donors.

In Africa, many countries face additional challenges that stem from the rapid pace of development in the for-profit private sectors. This growth gives the for-profit private sector enhanced sophistication, financial resources, and political clout. This influence cannot be matched by either the public sector—governmental regulatory agencies or research institutions—or the nonprofit private sector—NGOs or local community groups—without concurrent growth and evolution.

Comparable levels of sophistication in all sectors are needed to make civil society robust. Endowments can stimulate the development, and provide the means for effective work among independent organizations, businesses, and public sector institutions.

Both donors and countries share a need to find innovative ways to promote the sophistication and clout of key governmental agencies and nongovernmental institutions. Traditionally, foreign donors have supported and funded innovation in both public and for-profit private sectors. This source, however, grows less useful as aid levels drop. Endowments can help key institutions become an ever-renewing source of innovation.

HOW IS ENDOWMENT REVENUE USED?

An endowment provides a revenue-yielding asset that can give financial stability to a nonprofit organization. If the interest from the asset is sufficient to make grants, an endowment makes it possible for an institution to diversify its activities and build capacity of other institutions in the government or the nonprofit sector. A diversified activity base opens up opportunities for diversifying sources of support among local and foreign donors. A “captive” source of revenue-generating assets gives an endowment significant leveraging power for raising additional funds from potential donors.

Endowed institutions can build mutually beneficial bridges among the governmental, for-profit, and nonprofit sectors. Having community leaders from all sectors sitting on the board of directors of an endowed institution builds a bridge within the community. Investing endowment funds in local capital markets, where allowed by donor regulations strengthens the for-profit private sector. If those investments are large, then business will focus on the social and environmental concerns that the endowed institution is set up to address. Grants from endowment funds that support high-risk and long-term research and technology transfer can stimulate enterprise and markets. Endowments, with governmental help via tax policy reform, can provide a channel through which the for-profit private sector can address community and societal concerns.

Endowed funds can anchor a funding strategy for an institution. The income that they generate can either be dedicated to a specific need or program, or be used to smooth out variations in the flow of funding from other sources. Checkoffs, for example, where a producers' association contributes a portion of profits to a research institution to promote agricultural research, might be a preferred alternative for the bulk of funding for an agricultural research institution. But, in periods of low commodity prices, an endowment could keep research programs on a steady course. Selling donated birth control devices might be a way for a family-planning NGO to raise money, but when donations decline, an endowment could provide funding that would allow the NGO to broaden its fund raising to include direct appeals to individuals and corporations. In all cases, an endowment, because it confers stability, will make institutions more attractive to donors and more reliable in the eyes of clients.

Environmental Case

Since the 1992 United Nations Conference in Environmental and Development (UNCED) meeting in Rio de Janeiro, many countries have struggled to implement their National Environmental Action Plans (NEAPs). In most cases, governments lack the institutional critical mass and the budgetary resources to shoulder the responsibility for all NEAP-mandated programs. In such cases, the best alternative may be to create a new endowed foundation that is dedicated to building the institutional capacity to implement NEAP-mandated strategies.

Essential to the ultimate success of NEAP programs are sustained activities which require both continued financial support and maintenance of a critical mass of competent and dedicated human resources. Environmental sector projects, especially efforts to preserve biological diversity, need patient work by skilled persons in an atmosphere of steady financial and institutional support. By contrast, the longer history in other more traditional development sectors, provides a richer store of “lessons learned” about which approaches work. Relatively less experience in tackling environmental problems means that stability in the level of resources committed to a long-term goal, from problem identification through evaluation, occupies a prominent place among the factors determining success. At the same time, endowments place power over resources in the hands of those ultimately responsible for the sustained productivity of those resources.

Donors should work with host country governments to explore an endowment as an alternative to traditional ways of committing resources to environmental problems when either or both of two situations exist:

- existing mechanisms and institutions do not have sufficient reach and capacity to assure steady financial support over the long term; and
- elements of civil society—indigenous people, urban poor, traditional farmers and pastoralists—that are key actors in any effort to mount and sustain environmental management efforts, do not have any meaningful way to participate in decisions concerning use of resources.

Agricultural Case

Traditionally, agricultural research institutions have been supported through national government budgets, supplemented by annual donor grants. Since the end of the colonial era, agricultural research has continued to benefit from the recognition that:

- a broad program of agricultural research is essential to economic growth; and
- payoffs of investment in research come, for the most part, later than payoffs in other sectors.

The time-consuming process of agricultural research means that substantial institutions must be maintained and careers supported overtime to obtain the full benefits of these investments. The process by which agricultural research is conducted has remained more or less, fairly consistent over time. However, declining foreign aid has raised concerns about the continued viability of agricultural research institutions and the process by which research is conducted and supported.

Other factors are putting pressure on agricultural research. As economies grow more complex, there is a need to empower consumers—defined broadly to include both those who use new technologies and those who purchase agricultural products—by giving them a meaningful voice in setting agricultural research priorities. At the same time, in many other countries, agricultural enterprises are becoming a more influential part of the private sector.

As agricultural research institutions evolve as a result of gaining new and independent sources of funding, they will become part of coalitions based on a common interest in sustainable economic development. Agricultural research institutions need to be strong, independent and capable of debating and tempering private interests with public welfare and short-term growth with long-term viability.

Endowed institutions can also provide a greater number, and richer mix, of career opportunities for the growing number of highly trained agricultural professionals in the developing world. For example, since the early 1980s, donor investment in training has tripled the number of African agricultural scientists with Ph.D. degrees to approximately 4,500. Endowments can help to create a better funded and more secure institutional framework that can employ these professionals in responsible technical positions.

HOW INTEREST IN ENDOWMENTS EVOLVED

Since 1990, interest in establishing new endowments has grown rapidly throughout the world. There are two bodies of experience. One, primarily in Latin America, represents endowments for existing institutions that developed out of a need to create a new funding mechanism.

A second and more recent body of experience comes from a desire to make the funding of conservation programs—national parks for example—more secure over the long term. Driving these endowments is the growth of new or greatly expanded institutions that are capable of taking on much greater responsibilities. While differing in sequence and rationale, each experience offers lessons to the other, and each shows a need for access to the lessons learned.

The number of endowments is growing rapidly. However, several efforts have set a precedent, including one by the World Conservation Union (IUCN). IUCN's program to support endowments has begun a program to promote the concept of national funds in environmental sectors, typically with endowments. Building the "Global Initiative for National Environmental Funds" calls for increasing support from donors and governments. Their initiative describes eight possible attributes of endowments, which, depending on the way they are set up and managed, can be attractive to donors, governments, and civil society.

- **Participatory**: National funds encourage the participation of interested parties (government agencies, business sectors, and relevant interest groups) in all aspects of environmental projects. They become democratic and accountable nodes of empowerment capable of moving beyond narrow sectoral interests.
- **Representative**: National funds encourage the representation of diverse interests in common activities that require cooperation and shared control.
- **Ethos building**: National funds promote value systems that feature democratic principles, cooperation, and accountability, and move beyond the limitations of particular professions or sectors.
- **Robust**: National funds can be designed with multiple accounts and multiple sources of funding. Diversity encourages stability, growth, self-reliance, and independence.
- **The right level**: When developed at the national level, or, where circumstances warrant, at the regional level, environmental funds are at the most effective level for striking the balance among international, national and local objectives.
- **Growth with minimal displacement**: Because of their ability to deal with mul-

tiple sources of income and multiple clients, national funds help distribute large infusions of capital so that they do not build one institution or program at the expense of others, or result in "all or nothing" competition. This encourages greater efficiencies within the system, and greater net benefits overall.

- **Absorptive capacity**: National funds can accommodate donors' needs to move large sums of money with fewer staff, while respecting recipients' needs for stability, steady growth, multiple, and small initiatives, and long-term institutional growth.
- **Focus**: National funds create an ideal focal point for donor and recipient interactions. They jump-start long-term processes that encourage synergy among donors and recipients, create platforms of potential interest to an ever-widening spectrum of capital sources, and serve as vehicles for building local capacity for responsible decision-making.

NOTE ON RISK

Creating an endowed fund represents a risk in power-sharing. An endowment gives life to an institution beyond the three-to-five-year time frame of normal donor programs, the period during which donors can and do keep close oversight of activities. Donors and recipients of an endowed fund need to acknowledge the risk involved, and approach risk management as common responsibility.

The above list of possible attributes represents an ideal state that will require hard work to achieve. Those seeking to use an endowment mechanism must be aware that as the benefits of success are great, the possible consequences of failure are also magnified. Failure of an endowment, unlike the failure of traditional foreign aid projects, does not automatically die when a project winds down and the funding stops.

The key to avoiding "eternalizing" a failure lies in careful work among all the interested parties to create as many checks and balances as possible. Too often, endowment creators will be tempted to "clone" the structure of a developed country institution, such as a U.S. philanthropic foundation, and place it in an alien social, political, legal, and financial milieu. Creators cannot assume that checks and balances equivalent to the U.S. Internal Revenue Service, or public interest 'watchdog' NGOs can or should be approximated in another country.

ALTERNATIVE ENDOWMENT MECHANISMS AND CREATION

Endowment creators should carefully consider the following five key areas of concern before settling on a final alternative:

1) Purpose:
   What purpose will endowments serve?
2) Use:
   How will endowments' income be used?
3) Governance:
   Who has oversight on assets?
   Who has oversight on use of funds (grants)?
4) Assets:
   How are funds to be moved into endowments?
5) Creation:
   What process creates endowments?

A framework for analyzing the basic set of alternatives in each of these areas is summarized in Table 1.1.

Options offered in Table 1.1 are listed as alternatives in columns under the five key decisions that will determine the structure of the endowment as well as whether a new institution—an endowed foundation—needs to be created. Each alternative in Table 1.1 is more complex than the alternative listed above it and can be considered independently of any other aspect.

The alternatives in Table 1.1 are a basic set that would be useful in most situations. As such, this guide refers to Table 1.1 as a starting point for the analytical process of design and choice among alternatives. However, guide users need to realize that this set of alternatives does not exhaust all possibilities. The Bolivian government, for example, set up a fund whose board includes both governmental and nongovernmental representatives. This fund, "FONAMA", has special sub-accounts for each gift or donation from donors. These subaccounts act as a kind of restricted gift. FONAMA plans to add an endowment to what started as a channel for coordinating donor support of environmental projects in Bolivia.

TABLE 1.1. OPTIONS TO CONSIDER WHEN DESIGNING AN EDOWNMENT

A	B	C	D	E
What Set Of Purposes Will Be Served?	***How Is The Endowment's Income Used?***	***Who Has Oversight On Assets And Use of Funds (Grants?)***	***How Funds Are Moved to Endowment?***	***What Process Creates An Endowment?***
Define a goal with explicit task (e.g. managing a national park, educating AIDS orphans, funding agricultural research.	Budget Support for Programs implemented by the endowment's manager.	The management of an existing institution.	Debt swap (exchange rate leverage).	A partnership between an international NGO and a local group.
Set long-term goals, i.e., NEAP.	Grants to local NGOs.	The management of a new institution created for a specific purpose.	Non-project assistance or structural adjustment loan (policy leverage).	A national consortia of local NGOs.
Empowerment, (giving society the means both to set priorities and choose strategy.)	Grants to local communities.	The management of a foundation with a broad mandate.	Direct grant to an existing or new institution possibly for an account in U.S.$.	The participation of local communities.

2. Alternatives to Endowments and Foundations in Africa

ARTICULATING A RATIONALE FOR PURPOSE AND USE

Choosing among possible purposes—ways of using income—and an institutional home for an endowment, must have an explicit rationale. Endowment creators should be able to articulate a rationale that covers the following:

- statement of a mission;
- convincing argument that a purpose and an institution should be given "perpetual" life; and
- clear grounding in a national goal that has broad support in all elements of society.

These three attributes of a convincing rationale apply to all the alternatives listed in the first three columns of Table 1.1 (purposes, use and management). However, if endowment creators wish to consider the more complex alternative of creating not only an endowment, but a new institution to manage it, then the rationale needs to be expanded to cover additional questions. These questions arise not just because the task is more complicated, but because credibility as an independent institution, decision-making, and governance of the new institution will need to be vested in its board of directors and not with the donor source. Thus, at a minimum, clear expectations and explicit conditions about the use of the endowment for a specified period of time will need to be established during the creation process.

CHOOSING PURPOSE AND USE

The first step in creating an endowment is to distinguish between its potential purpose and use. Purpose (see column A of Table 1.1) and use (see column B of Table 1.1) answer the "why" and "how" questions respectively. A purpose is the stated goal for an endowment, such as supporting agricultural research, building environmental management capacity, or providing for the care of AIDS orphans.

Defining how endowment funds will be used requires determining the best strategy to achieve a desired long-term goal. The use of the endowment (see column B of Table 1.1) should address its intended purpose and be a cost-effective way to spend revenue given social, political, and economic realities of a particular country.

An Endowment for Orphans. To illustrate the relation between purpose and use, consider an endowment to help orphans. The endowment's income could be used to build and maintain an orphanage for 2000 children. But if a country faces the problem of helping several hundred thousand orphans by the year 2000, as does Tanzania because of parents dying from AIDS, then the endowment's income would have wider impact if it were spent helping local communities impacted by AIDS strengthen their capacity to help orphans in a community setting. If the endowment creators choose a strategy of working with others to leverage the impact of the endowment's income, then running a grants program becomes more complex because it involves a wider variety of organizations and client groups operating with different abilities to receive and use income from the endowment. In such a case, the creation process is necessarily more difficult.

Virtually all long-term sustainable development goals could be advanced by an endowment for a single purpose or for a range of purposes. The alternatives for an endowment's purpose in Table 1.1 range from the relatively inflexible, dependent, and straightforward, such as an endowment for a readily defined purpose, to the flexible, independent, and complex, such as an endowed, grant-making NGO foundation. Each alternative requires careful consideration in light of the alternatives for other key aspects of an endowment. This will result the ability to select an appropriate purpose and articulate the objective arguments in support of an endowment.

The middle alternative of the first column offers flexibility, but not necessarily independence of management. It could allow for the participation of community groups and other key elements in the development of program strategies and approaches, in response to national and local problems.

An endowed foundation, which relates to A-3 in Table 1.1, could provide funding with the support of a broad cross-section of society. This type of foundation could set not only strategy within given priorities, but also its own program goals. Once it achieved a sufficient size and reputation, it could influence the setting of development priorities and policies at a national level. If a nationally prominent role is desired, then such an endowed foundation will need a mandate from society to be able to function effectively in the "public interest" as a kind of national donor agency, to take a lead in convening public debate about sectoral priorities, national policies, and program strategies, and to have the stature to launch fund raising efforts.

Developing a broad societal mandate for a new institution is a complex and lengthy process. It requires widespread participation, including local community groups, in the process of establishing the endowment and institution. And a broad cross-section of society will need to understand and be ready to support the work of the foundation. Because work done in the preparatory phase is crucial to ultimate success of a newly created endowed foundation, choices should be based on thorough analysis of factors that relate to the initial suggested use of an endowment.

Long-Term Funding: Beyond the Project Cycle

Endowment creators may wish to start with the aim of making the support to key sectoral programs less vulnerable to changes in donor priorities, to shifting relations between host country governments and foreign donors, and to host country political and policy shifts.

A long-term goal may be to create an independent and stable source of funding for these programs. This goal can be reached by endowing an existing institution that has a positive and proven track-record, or by creating a new institution. The decision should be based on the presence of existing institutions that have similar organizational goals, and capacities, and desires to carry out the mandate on a national level. If a new institution is created, the governance structure and its base of legitimacy will be critical factors. For a new institution to be effective, the national environment (including the social and political setting) must be favorable. In either alternative, endowment creators will have to work carefully to avoid substituting a dependency on international donors to one on endowment income.

Innovative Mechanisms: Fostering Institutional Development

Sustainable development strategies and renewable natural resources conservation strategies require long-term and sustained support to find and nurture the behaviors and attitudes that regard resources as a trust to be cared for in light of the needs of future generations. The mechanisms may include decentralizing decision-making on the use of natural resources, strengthening NGOs and local community groups, and developing new and innovative partnerships among NGOs, local community groups, government agencies, and the private sector.

Short-term and fragmented support provided on a one-to-five-year project basis begins to address these issues. However, by definition it cannot address them completely, but an endowed foundation could. It could provide direct grants to local communities and to local NGOs and others, and help them identify resource problems, and develop plans and technical assistance. If these grants fund activities that require closer collaboration among local communities, NGOs and governmental extension agents, the foundation's support would create an indirect incentive for NGOs and governmental agencies to strengthen their field presence in order to fulfill their role in partnerships with local communities. It could pledge to long-term support.

An endowed institution would also need to support the institutional development of NGOs and local community groups and carry out key functions such as training, information gathering, and planning. These are the functions that international donors find it most difficult to fund because they are difficult to measure and because the funds are sunk into "process" activities rather than "product-oriented" activities.

However, strengthening the capacity of NGOs and local community groups is a prerequisite for these groups to be effective at the policy level. An endowed institution would be able to serve these two groups not only directly in the form of sustaining financial support, but also indirectly, through board-level decisions that set priorities for the foundation's approach to issues.

Achieving difficult to define and measure changes will require facing problems of conflicts of interest. These problems arise in many forms, including ethnicity and group affinities. Even careful attempts to "balance" boards and governance with representatives of major groups will not prevent such conflicts from arising. Balance must be bolstered with as many checks as reasonably possible.

Local Control: Promoting Innovation

If the purpose of an endowment is to provide support for innovative action, then procedural barriers to new approaches and methods of funding need to be minimized. At the same time, flexibility in management must not compromise accountability both to the peer community of local NGOs or to donors. No type of activity should be ruled out of bounds without clear reasons presented by donors that the NGO community can understand and accept.

The rationale for choosing among the alternatives in column B of Table 1.1 should comprise the scope of programming activities with several statements of general aims. For example, the endowment seeks to reach a broad range of NGO types and an ever-increasing number of individual organizations, or, the endowment seeks to develop NGO capacity in financial management, activity planning, and project direction.

If the endowment will be managed by an independent foundation, its use of the endowment would be subject to review and modification by the board. The decision on how to use the endowment represents the fullest commitment to the philosophy that participatory processes should have great influence on setting priorities. It also may lead to conflicts with donors that are more interested in specific issues rather than in the growth of local institutions dedicated to the grassroots determination of priorities. In such cases, the management of the endowed funds should be flexible enough to negotiate time-limited program restrictions on donor contributions to an endowment. This would give the donor agency assurance, yet not negate the principle of local control.

Increasing Participation Empowering Communities

If an endowment is to provide the most secure, long-term funding base, then it would be prudent to provide a funding base for local NGOs and local community groups that is independent of and complementary to funding resources available to international NGOs—foundations, corporations, and the concerned public of the developed world. Further, in light of the growing tension between NGOs over issues of program direction and management, donors could use endowments to balance their dependence on international NGOs as agents of the long-term development.

The process of forming a board for the endowment's management, which is necessary under those alternatives calling for a new institution, is crucial to the issues of participation and legitimacy. If this process is limited to a few individuals and is conducted in secret, then many might justifiably view the result as an institution under the control of a small, elite group. If the process is open to a broad range of groups representative of the community, region or country, then the endowment would begin its institutional life with more credibility, not only because more key groups felt a degree of ownership, but also because the new institution would start with a reputation for openness and accessibility.

Community foundations in the United States operate to serve the public good within a specific community. They endowments are managed by and for the people in these communities and seek to have an impact at a national, regional, or local level. They have a representative board of directors and established procedures for the use of endowment funds. There are community foundations dedicated to public education, local arts, community services, poverty alleviation, civil rights, and local social needs. Many were established by local philanthropists, others by church councils or social service organizations that serve as cooperative funding vehicles. Many have as an explicit purpose to empower disadvantaged groups.

Beyond endowment funds, other monies generally are solicited or received by the foundation staff and board from businesses, philanthropists, and other sources. The endowment fund's reputation is a critical factor in gaining community support, particularly from local donors. Board members are carefully selected from the community on strategic basis for their competence, reputation and interest in the work of the foundation.

MANAGING ASSETS AND MAKING GRANTS

The alternatives in oversight on assets and use of funds (see Column C of Table 1.1) differ more in their implications for management of grants than in management of assets to generate income for making grants. Therefore, the following section does not distinguish between the alternatives in terms of their implications for asset management.

Donor Responsibility in Tracking Grant Money

Before addressing the questions of how an endowment manages its assets and grants, endowment creators need to understand and define precisely their responsibility for oversight in the creation process and any continuing obligation to track funds. The aim of this process should be to foster the endowment's ability to manage its own affairs. Donors need to consider several degrees of oversight and a sequence by which a transition is made between them. The oversight process should be supported by a set of objectively verifiable criteria and a clear statement of roles and responsibilities for the board and staff of the endowment and the donor(s).

The most straightforward case arises if the endowment's assets come from the national government, which a donor supports as part of a policy reform program through a low interest loan or grant. As part of the contract with the donor, the national government agrees to an agenda of reform and other actions. Such concessional, non-project aid "frees up" an equivalent amount of local currency. The national government might agree to use its own, newly freed-up budgetary resources in furtherance of the policy reform agenda. For example, a national government might agree to increase the salaries of civil servants or increase support to an environmental agency, or, fund an endowment for either an existing or a new institution. Whatever the funding agreements are that are set by the reform agenda, a donor has no obligation to track the money beyond the conditionalities stated in the policy reform agreement.

In other cases, a donor may wish to contribute its money directly to seed an endowment fund. In this case, the donor might retain oversight on the use of investment income for a period of time comparable to the life of a typical donor project, such as five years. The donor and the national government should also agree on the degree of oversight, and the duration for which the donor would exercise oversight on the assets of the endowment. If feasible, the donor might also set a limit to this oversight, such as ten years. As an example, such an agreement might state that for an initial ten years, the endowment's managers would have to obtain the donor's permission to alter the nature of the investments of the endowment's assets.

Rather than being focused on a set time period, the donor could relinquish oversight on the endowment's use of interest income contingent on a successful track record of the endowment's activity during a defined period of time (such as three grant cycles). An independent evaluation can make this assessment for both the donor and endowment manager. In keeping with this approach, a donor's best strategy would be to find and nurture an indigenous organization that has credibility rather than create a new organization. Consulting among other potential donors will increase the likelihood of co-funding and stronger institutions.

Managing Assets: Investing Capital

The financial *raison d'être* of an endowment is to protect the value of assets while generating investment income from the use of those assets. Traditionally, private donors and bilateral and multilateral aid agencies focus on short-term projects of approximately five years, which often fail to have a lasting impact when the money runs out. Endowments can extend the commitment to long-term goals over a longer period of time, by tempering budgetary and political fluctuations. Fulfilling this objective necessitates acquiring and managing assets, so as to maintain their value and revenue-yielding potential.

Ideally, an endowment's assets should be managed to keep a principal intact, with net interest and investment revenue available to support project activities of local community groups and NGOs. An investment strategy and management plan need to be negotiated initially between donors and endowment managers. As a goal, an endowment portfolio should generate at least a four to five percent return, after adjustment for inflation and the cost of portfolio management. This level of asset management is possible in a few developing countries, but will prove difficult in many settings.

Numerous alternatives are open to the managers of an endowment's assets:

- deposits in local private commercial banks;
- holding government bonds or notes; and
- equity or debt of privatized national companies and real estate.

Limits on the mix should be determined at the time the endowment is created. In some cases a donor may place restrictions on where and how assets are invested.

Given unstable or nonexistent local currency markets, the value of the principal in perpetuity may force asset managers of endowments denominated in local currencies to step back from this goal. In this situation, managers would draw the endowments assets down over time—a sinking fund—and manage donations so as to stretch them beyond the normal donor life-of-project cycle.

Sinking Funds. In some countries, the financial, social or political climate may make the notion of an endowment in perpetuity untenable. In this case, the idea of a "sinking fund," might be a better aim. Such fund would use investment income to augment its initial assets to be able to fund a worthy purpose for 10 or 15 years. This is an intermediate structure between the perpetual endowment and a grant fund. If successful, then consideration could be given by a donor to "eternalizing" the institutional framework with another grant at a much later date.

Regardless of the state of local financial markets, building financial management capacity will pay off when local financial markets develop to the point where an endowment can be managed in perpetuity. An endowment's financial managers should anticipate the various pressures on an endowment's assets, including donor gift restrictions and reporting requirements of national governments and donors. Effectively anticipating and managing with these pressures will enhance the endowment's attractiveness to potential donors.

MAKING GRANTS A PARTICIPATORY PROCESS

If the endowment has a broad mandate to be responsive to changes in social, economic and resource conditions, it needs to operate in a manner that is flexible and responsive to local needs. It also needs to create opportunities for popular participation by stakeholders and constituent groups. These preconditions are likely to rule out a governing structure that gives veto power to a host government. However, this does not negate a host government's legitimate interest in how the endowed institution manages its finances or how grantees use its money.

Arrangement for the Dissolution of Endowments

Terms and conditions for the dissolution of the endowment should be agreed to as part of the process of establishing an endowment. This is crucial to the reputation of the endowment and its ability to raise additional funds. The plan for the disposition of the assets of the endowed organization must be explicit and agreed to by all parties in advance.

Achieving Credibility: Models for Governance

The selection process for the members of a governing board is of key importance. The board—whether an existing institution or a new endowed foundation—will be responsible for all decisions affecting endowment-generated funds, including personnel, investment, grant, and priority. It is ultimately responsible for maintaining good relations with all groups important to the endowment, including foreign donors, local and international NGOs, host governments, and the local and international private sector.

The major question concerning the board's makeup is how best to ensure that the board is free enough to rise above the web of obligation binding each board member, yet structured enough so that, as board members change, the overall composition of the board does not drift toward a particular viewpoint. For foundations to succeed, the organizers must create an "ethos" of service to society. The board must be dedicated to nurturing this ethos.

Alternatives for selecting a governing board are listed in the last column of Table 1.1. Two concerns should guide the choice of a board selection method: the need for accountability; and the need for independence.

There are several models that address both the composition and restrictions on and of the board, including the following three common ones:

- **representative**: members represent different interest groups or organizations;
- **self-perpetuating**: members elect their own replacements; and
- **restricted**: members occupy seats with different restricted qualifications.

These types of boards are not the only models, though they are the predominant ones. One important consideration in the structure of any board is to be able replace board members who have a demonstrated ability to think creatively with a minimal obligation to a fixed view point, philosophy or particular group. A board representative would likely tend to reinforce a member's obligation to the group.

Even if members were to be limited to only one term, the possibility of returning to its home group will exert a strong influence over decisions while on the board. On the other hand, a purely representative board would more likely keep the endowed foundation focused on understanding issues and priorities. If the groups chosen to select board members become marginalized within the local community of NGOs and community groups, the members would be less beholden to them.

Self-perpetuating and restricted boards expect their members to be less bound by old associations with particular philosophies. Self-perpetuating boards are be the freest in this regard, but over time and replacement, they can drift to extreme positions.

Restricted boards offer compromise between self-perpetuating and representative boards. The charter of an endowed foundation may specify seats on a board with special qualifications, such as experience of a minimum period in the community development field, residence outside the capital city of specific duration, or indications of leadership on particular issues as evidenced by published articles or speeches.

Although a few U.S. environmental organizations have boards elected by member groups, U.S. experience offers few examples of boards other than self-perpetuating it is wise to look to local traditions of self-governance for inspiration. Boards whose membership selection derives at least in part from local models may offer promise of wider acceptance locally; however, this gain needs to be weighed against the same need for international donors to see a recognizable structure from their own experience.

Whatever board structure and scheme is used for selecting board members, endowment creators need to address the issue of how broad a base of experience can be tapped. In essence, the question is: Does the endowed foundation derive its mandate only from NGOs active in the same sector as the endowed institution or from a broader constituency, such as stakeholders in a community. Stakeholders might include consumers, women's groups, local community organizations, agricultural exporters, labor unions, teachers, urban poor, or farmers. This broad range needs to be included both in the process of formal establishment (writing a charter) and in the initial and subsequent selection of board members.

The following suggestions are intended to raise issues which should be examined in the light of the need to find this balance:

- avoid drafting new national laws, but rather seek a special agreement with the national government (reflected in the charter and bylaws) to establish the rules by which the government oversees the foundation;
- government power to regulate foundation affairs should be explicit; the use of grant money conforms to national law;
- the foundation should maintain a transparent record of all actions, including agreements with governmental agencies and donors; there should be no secret files or reports;
- in advance of funding the endowment, agree by what process and by whom questions can be raised about foundation activities, and by what process the foundation can be dissolved and its assets redirected;
- have explicit requirements for reporting, both to the foundation by grantees and by the foundation to the public; and
- retain local legal counsel to assist in drafting the charter and bylaws.

Governing an Endowment. No matter how carefully crafted, an endowed foundation's prospects rest on the character of its organizers and board members. Attracting these people requires that the foundation not only offer the promise of creativity, but also fair, realistic, and effective governance. The way the foundation governs its own affairs, how the national government exercises oversight, and how donors influence foundation activities all contribute to the framework of governance. Together, this framework of governance and the character of the foundation's staff and board members, lay the foundation for the growth of a foundation ethos.

Over time, funding organizations will be able to see if this ethos has matured. The indicators can be determined clearly. One sign of maturity is if the foundation's structure and procedures promote the honest appraisal of priorities and proposals. Another is if the board members go beyond their personal "web of obligation" to support agendas and programs beyond their own interests.

While the ultimate responsibility for fair and effective governance rests with the foundation organizers and administrators, donors may take steps to encourage, or at least not discourage, the growth of good governance. Donors should help strike a balance between the strictness of procedures, on the one hand, and, the freedom of majority decision-making on the other.

MOVING MONEY TO THE ENDOWMENT

This section reviews the major alternatives for, and describes the steps involved in, designing endowments through a combination of alternatives (see Table 1.1).

Use of a Debt Swap to Fund an Endowment

In Africa and in other regions, many endowment creators and international NGOs have viewed debt-for-nature swaps as an attractive alternative for programming in the natural resource area. Endowment creators have favored working with international NGOs to establish a newly endowed foundation because international NGOs, for the most part, have the managerial and administrative capacity to account for the funds. Many offer complete services:

- arranging swaps with banks that hold the debt;
- coordinating with the host country Central Bank to exchange purchased debt for local currency;
- finding local NGOs to serve as counterparts; and
- managing local currency to support biodiversity and conservation activities that they and their local partner then program and manage.

The international NGO community has been particularly attracted to these swaps because of beneficial terms, such as leverage on the conversion of their funds to local currency, publicity, and opportunities to work cooperatively with Central Banks and private commercial banks that have traditionally not been actors in the conservation of biological diversity. Such "deals" have provided NGOs with funds independent of host country public sector control.

Donors interested in addressing environmental problems have not sought out many direct alternatives to the use of international NGOs as intermediaries in creating an endowment. Partly, this represents a bias toward the familiar as well as an absence of alternative, more direct channels to support projects and programs managed by local NGOs. And, in many, but not all cases, "debt-for-nature" swaps have been used to generate money in local currency.

Traditional debt swaps based on typical debt-for-nature transactions generally involve the steps in the following hypothetical situation (note that the steps are usually taken in chronological order, but variations are possible):

1. A donor makes available cash in a hard currency (say US$1 million) to an international NGO for the purposes of funding a sustainable development project in "Ruritania."
2. The international NGO negotiates in advance with the Central Bank of Ruritania for a swap **quota** (say US$5 million in face value of debt) that would allow the NGO to swap notes it would purchase for local currency obligations of the Central Bank at a set exchange rate. Note that this swap may occur in several tranches up to the total of face value as agreed to by the Central Bank.
3. The international NGO then goes to the secondary market in the debt of Ruritania to purchase Central Bank obligations from international commercial banks at the prevailing **market discount** of 60 percent in Ruritania (i.e., buys notes with a face value of $2.5 million for 40 percent of the face value).
4. The international NGO then swaps the notes for local currency obligations of the Central Bank, often at a **redemption discount** on the official exchange rate, say 20 percent, and often with staggered dates of maturity and interest. As a result, the international NGO gets a cash and obligations worth $2 million in the local currency of Ruritania.
5. The international NGO then turns over the local currency proceeds of the swap, whether in cash or **Central Bank bonds** to its counterpart local NGO; the local NGO may or may not be an affiliate of the international NGO for the funding of program activities. In a typical "debt-for-nature" swap, these activities might include: surveying biological resources of particular note; determining what land is worthy of being designated as a national park or protected area; buying

land found to be prime habitat for endangered species; setting up park management plans; sponsoring research into endangered species and their habitat; paying for the services of park rangers and guards; educating the public about conservation; training park staff; employing local residents as guides and informants.

6. If the money needed, (say only $250 thousand worth of local currency), is less than the amount proceeding from the swap, then the rest ($1.75 million) may be put into a bank to earn interest. Such an account might be managed as a sinking fund which is slowly depleted over several years, or as an endowment, where only the net interest earnings are spent each year.

Each participant benefits in a debt swap: donor gains a bigger impact from its grant through leverage of secondary market discounts; international NGOs gain funding and valuable free publicity from arranging a swap; Central Banks retire debt; and the local NGO's partner or affiliate of the international NGO gains support for its program activities.

Dealing with Inflation: AssetTransfer

In either approach to endowment creation, a donor and an international NGO, if involved, will negotiate with the host government over terms of the endowment. Traditionally, in a debt swap the international NGO deals directly with the host government's Central Bank to set the terms of the swap, (i.e. the discount rate and the period of maturity of notes if it is not a cash transaction). A concern of the Central Bank is the inherent inflationary impact of a swap because it involves an increase in money supply. The donor funding the swap is often indirectly involved in these negotiations as a member of the donor committee for the host country.

Donor committees usually follow the lead of the International Monetary Fund (IMF) and the World Bank in placing a high priority in the development of sound fiscal and monetary policies. Such policies include:

- maintenance of low inflation of domestic prices;
- a stable money supply;
- sound Central Bank policies; and
- movement along a path toward fully tradable currency.

If a donor pursues a policy reform alternative, then the host government might favor an endowment established with assets that combine cash and notes of the Central Bank. One scenario would be for the Central Bank to issue notes that have a staggered series of maturities lasting several years. To protect the endowment from loss of value of the notes, the Central Bank would pay interest at a rate several points over the rate of domestic price inflation, as published annually by the World Bank. This rate, called the indexed rate, would be set in the agreement and in the notes themselves. Notes can be assigned in order so that the endowment may be able to sell them or deposit them with a local private commercial bank as loan collateral to raise cash if needed in advance of the maturity dates. Being assigned also affords more protection against default in payments.

If a debt swap alternative is favored, one way to minimize inflationary impact is for the swapping NGO to purchase the foreign debt of a large company, such as the national telephone company or electric power company. Because this debt is often guaranteed by the Central Bank, it usually sells for the same discount rate in the secondary market as the sovereign debt of the Central Bank. Consequently, the Central Bank would still have to approve a swap, but swap arrangers could finesse the inflation question by swapping the debt, not for local currency, but for equity in the private company. These share holdings would then immediately become the endowment's capital. As the endowment needed cash, it could sell the shares for local currency. The net result would cause little pressure to increase the inflation rate.

A similar swap may be arranged in countries where the host government is in the process of privatizing national companies. As part of the privatization deal, the endowment could be given holdings in the publicly offered stock of the newly private company, in exchange for foreign debt purchased at a discount.

Limitations of Debt-for-Nature Swaps as Programming Tools. Recent experience primarily with debt-for-nature swaps has highlighted some of the limitations of debt swaps. There may be a lack of buyable (scheduled) debt at the time the purchaser, who will set up the endowment, has funds for the purchase. Administering and managing a sudden large infusion of local currency can cause problems which, if not handled appropriately, can have an inflationary impact. Criticisms have also been leveled against these endowments because they have not created a sense of buy-in from the local community where endowment funds are supporting new activities, (a particular problem in protected area conservation and development schemes.) There is a growing perception that "sustainable development" is really a code word for concealing a foreign agenda of: perpetuating a senior-junior relationship between international NGOs and local NGOs; and, getting around civil service reforms.

An apparent pitfall in debt swaps is that the technicalities for executing the swap have tended to take precedent over the patient and less glamorous work of program development. The negotiations necessary for arranging a debt swap must take place according to the pace of business of the international banking community and in response to market opportunities to obtain a favorable leverage in a debt purchase. In other words, the process of making a swap can drive the program that will be funded by the swap, rather than the reverse. In such an atmosphere, it is difficult ensure that the process will provide local communities with a sense of ownership and control.

The stated aims of a proposed swap and the programming alternatives for local currency should be carefully analyzed by the entity that provides the funds for the purchase of debt. The use of a direct grant (i.e., keeping funds in dollar accounts) or a government grant linked to a policy reform process, may offer a preferable alternative if the aim is to build an institution with widespread participation in advance of funding.

Another alternative is to wait to consider a debt swap until after progress is made in the process for establishing an endowment for a new institution. Since this could take several years, the choice of a method for creating a source of local currency may not be on the table until after the optimal secondary market opportunity for purchasing debt has passed.

Using Policy Reform Conditionality to Create an Endowment

Because the process of writing a program document for policy-based aid follows a sequence parallel to the writing of a traditional project paper, there is ample opportunity to explore a process for the use of freed-up local currency funds. The process is similar to a debt swap, there are multiple parties involved, and local currencies are put in an endowment managed by a local corporation. However, a major difference of interest to donors is that instead of currency leverage of a debt swap, donors gain policy leverage of reform-linked aid.

In a policy reform-linked endowment, the host government agrees to give its own local currency to the endowment. These revenues, had originally been budgeted for the purchase of foreign exchange to pay debt service. As these local currencies are not generated as the direct result of a donor grant, the donor has no fiscal or programmatic responsibility over the use or accounting of these funds.

Again, using the hypothetical country of "Ruritania" as example, a policy reform-linked endowment process follows these steps:

1. The donor offers a hard currency grant or concessional rate interest loan (say US$20 million) to Ruritania with the intention of making the grant conditional on a series of policy reforms in a particular sector, natural resources, for example.

2. As part of the reform agenda, the national government agrees to work with local NGOs and community groups to develop a plan for an endowed foundation or institution. This institution would provide long-term support for a key need in that sector, such as agricultural research or capacity-building of the national park service. As part of its counterpart contribution to policy reform, the national government agrees to donate $5 million worth of local currency funds to the foundation for its endowment.
3. As a part of the policy reform agreement, the donor and the Government of Ruritania would set out the terms under which Ruritania's Central Bank would agree to give cash or notes, or a combination of the two, to a new entity when both the national government and the donor certify that the new entity has met established criteria.
4. The donor would also commit to fund (or arrange funding) for technical assistance, for a period of approximately three years, to work with the local NGOs and community groups to develop a plan, a charter, an administrative structure, and a board of directors for the endowment. The source of the technical assistance would likely involve professionals experienced in working with local NGOs and individuals from the international NGO community who are concerned with issues in the sector where the foundation would be active.
5. Under the terms of the policy reform agreement, the donor and the national government could require that certain program areas be given primary attention. For example, if the foundation intends to work in the environmental and natural resource areas, then the foundation might give priority to the implementation of Ruritania's NEAP. However, such restrictions should be broadly defined so as not to limit the new foundation's board in developing its own approaches and goals. To extend and enhance its programs, the new foundation should be able to accept donations to its endowment in either foreign exchange or local currency. Host country tax law may need to be reviewed and reformed to encourage this fund raising; the potential for raising additional funds will serve as a powerful incentive to maintain high standards of accounting and administrative control.

Use of Direct Grant

Possible other approaches combine aspects of a debt swap and policy reform conditionality. The variety is limited only by the creativity and openness of the process of negotiations between a donor and the host government, and by local restrictions.

ALTERNATIVES FOR SETTING UP AN ENDOWMENT

Concerns are likely to arise in the course of designing an endowed foundation (see Column E in Table 1.1). Every institution-building project must address many of the following familiar concerns:

- potential to drain human resources from other critical efforts;
- setting up reliable, but not burdensome, accounting procedures;
- minimizing rivalries within the nonprofit sector;
- conflicts between international and local NGOs on leadership;
- dependence on decreasing donor aid; and
- struggle for greater democracy and community participation.

Choosing a design is the first step of the endowment creation process. There is no need to differentiate between the process of choosing a design and setting up an endowment. In this case, NGO and community participation is critical in the discussion of alternatives for the institution to be developed or acquire its mandate from the nongovernmental community.

Any proposed approach to establishing an endowment will require that a number of groups— the host government, local NGO community, foreign donor community, and local private sector—be involved and become active supporters of the effort. An endowment cannot be designed in isolation from these groups; their involvement is key in the design and board selection, and in the institutions's role. Other groups may have roles, too. These others groups include international NGOs, multinational corporations, and philanthropic foundations.

Selecting Among Alternatives

Table 2.1 frames the issues to consider when designing an endowment. Major groups participating in the design discussion are listed along the left side of the table, and the areas of concern are listed across the top of the table. Each box raises illustrative issues that should be considered as part of the design process.

Three major questions involving people, money, and governance will arise in discussing how to create an endowment, whether for an existing institution or through the creation of an endowed foundation.

- **People:** Human resources development and manpower allocation have been the traditional concerns of donors and governments. In most countries, the lack of skilled persons limits the growth of new institutions. Even in situations where the number of skilled persons is sufficient, often the need for advanced training, whether degree or non-degree, limits the pace of development. And, highly educated personnel often migrate to more developed countries because it is often difficult to find challenging positions in developing countries.
- **Money**: Maintaining adequate accountability for project management requires constant attention. There is a tension between the need to have enough flexibility to pursue creative ideas, and the need to have reliable systems for accountability. This section emphasizes innovations which have built-in incentives to establish and maintain accountability.
- **Governance**: Endowments are operated within a framework of rules which are set by donors or contributors of gifts, the host government, and the charter of the endowed institution. The key feature which distinguishes an endowed foundation and allows, even requires, it to behave in ways which are unlike traditional NGOs or other public sector institutions, is its ability to change its own rules, negotiate restrictions with donors, and advocate reform of national policy. The issues raised in Table 2.1 are arranged by groups (listed along the left side) which have important roles to play and by areas of concern (listed across the top).

Relation to Government

Endowment creators should be careful to avoid draining off critical skills and talent from on-going and critical government programs, and NGO activities and projects. Design teams should be instructed to justify salary levels and the number of professional staff, in the context of prevailing rates and manpower shortages. If an endowed foundation is created as part of a policy reform program, then it is possible that the issue of civil service salaries would be a subject of analysis, as part of the policy reform agenda.

The tax status of earnings which an endowed foundation receives on investments, is a critical aspect of the relationship between an endowed foundation and the host government. In some countries, it may be possible to use the policy reform process to create a more favorable tax climate for all types of endowed institutions. National governments which are persuaded of the value of a strong and creative nonprofit sector should be willing to consider broad and clear guidelines for the income-earning activities of the endowed institutions. In others countries, the tax arrangement may have to be negotiated on a case-by-case basis.

Government's Role. Early in the design process, donors and other involved should obtain the host government's commitment to the establishment of an endowed foundation. If a donor can get a solid expression of support, then an early effort should be made to review national laws and regulations governing the nonprofit sector. The goal of this review is to define, as clearly as possible, the current regulatory and legal framework as well as its influence on the activities of local NGOs and community groups. If this framework is influential and would likely limit the activities of the endowed foundation or its anticipated community of NGO grantees, reforms will be needed. Reforms might address a series of issues that rise out of operations of nonprofits, including endowments. Review should explore aspects of current and desired relationship between government and nonprofits, including endowed foundations and other institutions. Most national governments will have definite, but not necessarily clearly declared, views on types of activities and range of issues that are acceptable for nonprofits.

Relation to Local NGOs and Communities

Endowments create good relations with local community in several ways. First is to include a broad range of groups in the formation process. As described above, an endowed foundation's credibility rests on its mandate. To preserve this mandate, an endowed foundation should seek ways to increase opportunities to work with local communities.

To build working relationships, an endowed institution can create mechanisms for broad input into the grant-making process. In a peer review, representatives of groups have an opportunity to evaluate and advise on proposals submitted to the foundation.

Another method would be annual occasions for public comment on an endowed foundation's funding priorities. The model for this participatory governance might be a town meeting, in which every person who attends has an opportunity to speak.

Relation to Foreign Donors

From the beginning, foreign donors play an important role in the affairs of an endowed foundation. Most critical is their technical assistance to help establish an endowed foundation. In identifying appropriate consultants to build foundations emphasize the institution-building aspects of the work rather than technical program-related environmental and technical skills. The purpose of the technical assistance, whether to help set up an endowment for an existing institution or set up a new institution around an endowment, is to identify an interested community at interest and be certain that newly empowered institution mirror community concerns and priorities.

Whatever route is chosen, donors should be careful that the personnel providing technical assistance is not strongly identified with a particular philosophical viewpoint. If there is a built-in bias, local communities might believe that an endowed foundation is not able to forge a local consensus on priorities.

After establishment, an endowed foundation must have procedures to manage and account for funds that satisfy requirements of potential donors. During early technical assistance, foundations could explore alternatives for satisfying these requirements, so not to overly burden an endowed foundation's administrative capability.

Another potential area of contention between donors and an endowed foundation is the desire of donors to put restrictions on gifts. Early technical assistance should examine alternatives for a clear policy on gift restriction. Policy alternatives include limiting life of restrictions, percentage of a gift that can be restricted, and types of restrictions, and pushing donors to focus on the funding process rather than subject areas to be funded.

Relation to the Local Private Sector

An endowed foundation's relation to the local private for-profit sector offers a great deal of promise for innovation. There has been little effort to have local private businesses play a constructive role in dealing with issues that endowed institutions are being created to address. There are several ways an endowed foundation can help build a bridge to the local private sector.

One approach is to seek out local business persons that are dedicated to sustainable development and recruit them for the board of directors of an endowed foundation. Local businesses in countries with a large private sector can become contributors to an endowed foundation. However, if this becomes a major source of funding for an endowed foundation, national tax law will probably need changing to provide incentive for charitable giving. Such a review could be a part of the technical assistance.

Tax Reform Issues: An endowed foundation is a special type of nonprofit; it holds assets and is expected to manage those assets to provide a steady and increasing amount of grant money to its target beneficiaries. A key to success is the development of laws and regulations that exempt endowed foundations from paying taxes. Tax exemptions to endowed foundation need to be determined on a case-by-case basis in each country. National governments and foundation organizers need to agree on statements of activities that can be support.

A second tax issue relates to laws that regulate gifts from local corporations and persons of wealth. In many countries, it may be feasible to establish tax deductions that encourage domestic corporations and individuals—as well as foreign companies operating in the host country—to make gifts to the endowment. If it is determined that there is a need for tax reform, then a donor should be prepared to work with the host government to develop a reform agenda, as either part of a policy reform agreement or through follow-on technical assistance. To avoid simply copying a developed country's tax and regulatory framework, this agenda should tailor its recommendations to specific conditions of the country.

No matter which alternative is chosen, the charter of an endowed institution can help the private sector in a variety of ways become more supportive of national sustainable development. Many parallel how U.S. foundations work with the private sector, but many are different; complicated interactions between nonprofit and for-profit private organizations in the United States reflect unique social and political context. Examples include support for research and development; feasibility study support; program related investment; no-interest loans; and, endorsements for marketing arrangements.

Developing countries vary greatly in the vibrancy and depth of private entrepreneurship. A strategy to help local, socially beneficial, "green" businesses must be tailored to local conditions. In a country with a strong private sector, provision of a limited amount of credit may begin to stimulate business interest. In countries with nascent private sectors, there may be justification for committing substantial resources to feasibility studies. In either case, an endowed foundation could provide more than token support for the private sector.

The private sector can become an important vehicle for tackling national development needs, if an endowed foundation has programs that enable it to influence the flow of local private capital investment. Without such influence, an endowed institution would miss an opportunity to bring in important determinants of national development that are the collective impact of a wide variety of for-profit activities.

Technical Assistance for the Design Process

Donors may have to commit to a substantial amount of technical assistance at all stages in the design process. However, the sequence of the technical assistance required may differ. In addition, requirements for donor oversight, both management and administrative back stopping, may vary in timing.

If donors make the initial decision to consider an endowment, the choice of alternatives is a crucial step; it will set the process on fundamentally different paths which have implications for what kind of endowment is eventually built. Donors may well seek help from consultants in making that choice. Consultants that donors select should be as free as possible from conflicts of interest.

One possible conflict to avoid might come from retaining an NGO that is in business of arranging debt-for-nature swaps, for initial work of characterizing and choosing among alternatives. Donors should also make sure an individual does not have an extensive history of work for an NGO that stands to gain from the choice of alternatives. However, such NGOs can be valuable sources of expertise that donors can tap if a local process yields priorities that are appropriate to an NGO's area of interest and experience.

If donors avoid the appearance of conflict of interest, they will find that obtaining support of local NGO communities will be much easier, because the communities will feel that they are on an equal footing with foreign NGOs at the beginning of the establishment process. Maintaining this favorable climate must be the prime responsibility of consultants that donors hire for the next phase, negotiating an agreement with the government.

TABLE 2.1. ISSUES TO CONSIDER WHEN DESIGNING AN ENDOWMENT

	People	Money	Governance
National Government	Will a new, endowed foundation drain skills from government?	Will an endowment need a special agreement with the government to avoid taxes on earnings of its investment?	What oversight does the government have on the use of endowment funds?
Local NGOs and Local Community Groups	How can local groups participate effectively in the formation of an endowment?	How can local groups participate in grant making, monitoring and evaluation?	How can the endowment set an example for transparency?
Donors	What are the best ways to provide technical assistance, as free of bias as possible?	What are the requirements for documentation of the use of funds?	What policies should guide restrictions on gifts?

3. Steps to Starting an Endowed Foundation

PROPOSED SEQUENCE OF TECHNICAL ASSISTANCE

This section discusses sequence of activities or steps leading to the creation of a grant-making foundation with an endowment fund. Other processes, such as that for creating an endowment for an existing institution (such as an agricultural research institute) will involve some, but not all, of these steps. In any case, the list given is illustrative. Endowment creators need to see that reaching agreement on the sequence of steps is an important part of the early phase of creation. However, a consensus must be reached among those with an interest in the kind of goals that the endowment might serve.

The process starts with an agreement among interested parties on how to obtain the broadest possible participation. This is a critical consideration if the goal is to establish a foundation greater than the interests of the donors, who contributed the initial endowment funds. If an NGO consortia exists that is representative of the needs and priorities of local community groups, it should be involved at an early stage. Its role could include promoting discussion among the NGO community and local community groups on the foundation concept. The following will spur discussion between NGOs and local communities.

Step 1: Secure Agreement on the Role of Local Community Groups and NGOs

An initial agreement to explore creating a foundation should be between the national government and a donor. However, if the foundation is to be an indigenous nongovernmental institution, the first concrete proposal would more appropriately come from the local NGO community or government, or jointly from a meeting of representatives of that community and the government.

The initial proposal will need strong identification with a constituency and community-based NGOs. It should include an agreement on the sequence of steps to create a foundation. For purposes of credibility, this agreement should cover in detail the first two or three steps described below, with subsequent steps characterized in broad terms. However, participants should thoroughly work out the process for agreeing on subsequent details.

The NGO sector is weak in many African countries. In fact, strengthening the NGO sector is a common goal in many of the pioneering African endowments.

The public sector, especially in parastatals and university-based research institutes, may offer the best potential for locating future leaders who can build the capacity of the NGO sector. In some cases, such parastatal organizations may offer the best place to incubate the process of creating a new institution with an endowment.

Step 2: An Organizing Committee — Selecting a Board

If local NGO consortia decide to play a leadership role in the foundation creation process, then a group or groups of local NGOs might start by proposing a way to govern the process.

This process will most likely need to be guided by the donor or a small group that includes donors, community representatives and, if appropriate, the host government. This group will act as a nominating committee. They can solicit the candidacy of individuals for the organizing committee. For credibility, the committee should be broadly representative of the ultimate constituency base, and represent the values of the foundation, dedicated to environmental concerns, broad social equity goals, and community development.

Overseeing the selection of the foundation board is the final act of the organizing committee. The board is responsible for finishing the following creation process:

- adopting the charter and bylaws;
- choosing alternatives for asset management;
- seeking formal registration of the foundation from the national government;
- planning programs;
- establishing administrative procedures; and
- when assets are transferred, making the first grant(s).

Selecting an organizing committee could take two to six months. Once established, the committee should immediately begin the process of hiring an interim coordinator.

The organizing committee should have clearly defined duties, including:

- hiring interim coordinator;
- overseeing regional forums for discussing foundation concept;
- agreeing with donors on nature, extent, and timing of needed technical assistance;
- choosing technical assistance;
- ensuring broad participation in drafting foundation's charter and bylaws;
- preparing communications documents; and
- overseeing process of selecting a board.

Step 3: Retain Interim Coordinator

The organizing committee is responsible for finding an interim coordinator. Several considerations argue strongly that this person should be a local citizen. A foreign interim coordinator would project the image of foreign donor-driven and created foundation. On the other hand, a local person would be more likely to understand local political currents, both inside and outside the NGO community.

The donor may or may not participate in the selection of the interim coordinator, depending on the terms of the initial agreement. If the donor funds the interim coordinator, then the donor may want input. On the other hand, should the organizing committee use other funds, then the donor may not have input.

The organizing committee will need support for its expenses, such as costs for the interim coordinator, regional meetings, newsletters, and media. The organizing effort will need grant support, which the organizing committee could seek from another donor, or a U.S. foundation. Having such a grant would give the local NGO community a small, but perhaps crucial measure of independence as it works with the donor during the creation process.

The interim coordinator's duties include:

- promoting participation in creation process;
- staffing work of organizing committee;
- preparing communications materials for internal and external audiences;
- promoting public discussion; and
- working with donor-supplied technical assistance.

The interim coordinator will stop work before the organizing committee transfers management to the board. A technical assistance grant gradually assumes costs of continuing activities of the interim coordinator. An alternative might be having the interim coordinator continue until the board is formed. In this case, the technical assistance grant presumably could pay the costs of the interim coordinator.

Step 4: Hold Regional Meetings of NGOs and Local Community Groups

During the first year of work, a key goal is broadening participation in the creation process. The organizers could hold a series of regional meetings in which they present the foundation concept and solicit ideas from local groups and communities. Issuing newsletters in local languages as well as newspaper articles will help this process. It seems efficient if the interim coordinator, with oversight of the organizing committee, manages this participation process.

Step 5: Provide Technical Assistance

Donors should declare a willingness to provide both long-term and short-term technical assistance to support the creation of a foundation.

The technical assistance might supply one long-term, (18 months or more), person who should either serve as the interim coordinator or work closely with the interim coordinator. The technical assistance could pay the interim coordinator. The interim coordinator could also continue to be paid by funding sources used to hire the interim coordinator initially.

If the technical assistance includes the role of the interim coordinator, selection of the interim coordinator could involve participation of the organizing committee. In other words, the organizing committee could have an equal vote in evaluating the qualifications of proposals for technical assistance. Under this alternative, activities of the interim coordinator would not begin until the technical assistance is in place.

Step 6: Prepare Charter and Bylaws

Approximately midway through Step 4 (holding regional meetings), the process of drafting a charter and bylaws should begin. This process will require skillfully interweaving two different sources of ideas and constraints:

The first source represents technical expertise, which would come equally from outside as well as from inside the country. Such expertise includes financial advice and planning, legal advice, administrative structure and procedures, and the experience of other foundations.

The second source represents the results of public discussions that involve as many different local groups and communities as possible. All sources of ideas need to be melded into a coherent whole.

The organizing committee should supervise the interim coordinator and the technical assistance in the drafting process. The aim is to write a charter and bylaws acceptable to all entities, including local community groups, NGOs, foreign donors, and national government.

Organizers should allow one year for this process; this will allow time to tap all sources of ideas and technical knowledge. After reaching consensus, selecting a board, and adopting the charter, organizers will submit the charter and bylaws to the government to secure recognition of the foundation as a nonprofit entity under national law.

Step 7: Review Alternatives to Manage Assets

The organizing committee needs to examine all alternatives for managing the foundation's assets. This analysis should continue after the board is in place, to allow the new board the opportunity to exhaust all questions and alternatives. Once the new board chooses an asset management plan, a continuing need would exist for financial advice. The board can obtain this advice via a retainer contract with a local firm, backed by an international firm.

Step 8: Register Endowment—Transfer Assets

Once in place, the new board would make a formal request to the government for registration as a nonprofit association. This registration may involve negotiating special privileges for the foundation, including, but not limited to, tax reductions on earnings and imports and tax incentives for donations from local private individuals and corporations. This process may take up to three or four months. If the organizers choose to register the foundation as an association of public interest, this process could take much longer. After a foundation completes this step, the national government can transfer the first tranche of assets.

The transfer of funds cannot take place until all previous steps are either complete. If during the early steps, it becomes apparent that delays would prevent meeting a date for fund transfer, organizers will have to revise plans and budgets to accommodate the extra time needed.

Step 9: Hire Staff, Plan Program, Make First Pilot Grants

The interim coordinator should work under the guidance of the board to recruit staff and work with local groups to plan the first grants program. This can take six to eight months or longer. To the extent possible, hiring staff and launching a program should take place at least six months prior to the first round of grant distribution.

Determining shape, approach and priorities of the first grant programs will present the foundation with the first test of its ability to function in accord with its goals. From its inception to Step 9, grant use, potential grantees, and grant structure will be at the core of all discussions. Here are some suggestions to help focus discussion:

- develop explicit criteria for grant eligibility;
- create a transparent process for arriving at criteria and quotas;
- create clear and simple guidelines for proposals, review process, monitoring, and reporting;
- encourage rapid review of proposals by the board;
- specify objective verifiable indicators that balance ethnic and geographic affiliations;
- develop programs that assist illiterate and inexperienced local community groups and NGOs in writing proposals and administering grants;
- develop an aggressive media campaign to build awareness of the foundation's purpose and activities;
- stress that staff keep exemplary records and conduct all work in a transparent fashion; and
- create explicit procedures for addressing conflicts of interest.

Many of the above suggestions will only be effective in practice if the new institution emphasizes peer reviews. To be effective, peer reviews need several precondition:

- precedents showing fair play;
- available experts that are qualified;
- incentives and a willingness to disclose interests in decisions at hand; and
- presence of an independent way to "review the reviewers."

As donors gain more experience with endowments and the number of endowments increases, need (and ability) to cooperate on programs to strengthen peer review will also grow.

Supplying Technical Assistance for the Establishment Process

For a foundation to succeed, its form, programs, and priorities must flourish under local control. An overall recommendation is to pay careful attention to the type of organization (whether nonprofit or for profit), contracted to supply the technical assistance so as not to compromise the principle of local control.

While creating a functioning endowment secures technical assistance, a key strategy toward achieving this goal is assisting local NGOs in their process of creation rather than creating an institution and turning it over to local management at the end of the creation process. Technical assistance needs to be provided in a way as to minimize an donor imprint. This will have two real benefits: local society will feel a greater ownership of the resulting institution; other donors, both bilateral and multilateral, will be more likely to provide funds for further institutional and program development.

An effective technical assistance plan requires a combination of local and foreign technical expertise. The technical assistance serves a dual purpose: to assist the creation of the endowment/foundation, and to build local capacity to manage the foundation's affairs. This capacity must include expertise from other local consulting firms, accountants, lawyers, and financial advisors. To this effect, the technical assistance strategy should pair whenever possible local expertise and foreign expertise.

As several endowments in different countries begin to take shape, there may be an opportunity to form a network for sharing experiences. Such a network could make available key persons from one country to another.

If the network grows, it may be worth using the network as a vehicle for a variety of technical expertise. In essence, the network could function as a kind of secretariat for promoting cooperation among developing country foundations and for building a body of experience and expertise needed by foundation pioneers.

A technical assistance secretariat—if it were under substantial control of the emerging community of foundations—could provide a buffer protecting foundation organizers from donor pressure and manipulation. It could also provide a channel for multi-donor support of the creation process.

RECOMMENDATIONS FOR PROPOSAL ASSET MANAGEMENT

The following steps—not necessarily in order of importance—summarize key recommendations for an approach to asset management.

Step 1. Develop A Realistic Asset Management Plan

A plan should provide financial support from endowment income for anticipated staff administration and program expenses. This plan must address a range of issues, including explicit strategies for managing the investment risks, ratios of liquidity needed to provide security for both staff and grantees, and explicit fund raising targets to maintain the endowment's value.

Step 2. Establish A Core Endowment Free Of Donor Restrictions

Despite the desire of many donors to restrict the use of their gifts to a foundation, a foundation will need to seek, and set apart in a separate account, irrevocable contributions. This account will provide the foundation with an unrestricted, internal funding source. These core funds will help leverage negotiation with other donors on joint programs.

Step 3. Establish Sub-Accounts For Restricted Gifts

Many donors will limit the use of their gifts to specific purposes such as the management of a national park, promotion of public awareness about soil conservation, or women's roles in sustainable agriculture. In addition, some donors may specify certain reporting requirements for their contribution. In these cases, a foundation should create sub-accounts with explicit provisions to address donor restrictions. These provisions may include clauses allowing the donor to suspend or cancel the gift and receive the remaining balance.

Step 4. Raise Funds From In-Country Sources

While the international donor community will probably contribute the majority of funds, a foundation will need to develop alternative funding sources, in the event that donors reduce their support. Such a strategy will promote self-sufficiency. While some foundations may raise funds from private citizens and local businesses, a more likely source lies in partnership with government. For example, a government could dedicate to the foundation user fees at a national park or special tourist taxes.

Step 5. Adopt An Asset Management Charter

A foundation's charter should describe the foundation's assets and their origin. Such a plan should project other sources of support, including bilateral and multilateral contributions, charitable donations, bequests and legacies, government grants, foundation grants, tax revenue and user fees, membership fees, dues and assessments, and investment income. The plan should specify what percent of total support will come from various sources and the type of fund raising activities contemplated. The plan might set a specific limit on the portion of annual budget devoted to administrative expense or have a minimum devoted to training. On the basis of this plan, anticipated staff expense and initial programs, the foundation organizers should determine the minimum endowment necessary to justify the expense and effort of creating a foundation.

Step 6. Establish A Board Finance Committee

A foundation's board should establish a finance committee that will set investment policy, retain investment managers, oversee investment managers, hire outside auditors, review audit reports, and prepare budgets, long-range plans, and annual fiscal reports. The investment policy should identify objectives, funding needs, and tolerable risk.

Conventional wisdom suggests that the policy seek long-term investments, strive for stable income that will support slowly growing funding needs, try to preserve the real value of capital, and emphasize conservative investments of lower risk. Highly unstable economies, however, may necessitate other policies. In any case, diversification of investments represents a good strategy. The finance committee will have to determine the best asset mixes that offer the highest return for risk.

Step 7. Define An Explicit Conflict Of Interest Policy

A foundation's board of directors should fully disclose their financial interest and refrain from discussing and voting on investment decisions that could affect their interests, or the interests of their families and business associates. The directors should set similar policies for contracts and procurement.

Step 8. Retain Outside Investment Managers

Choosing an investment manager will be an early board decision. At the same time, the board needs to set clear procedures for oversight of the manager's work. For example, the board or the finance committee may want to reserve the right to approve any investment decision above a certain amount, but allow the outside manager to shift assets within clearly defined limits.

References

Economic Commission for Latin America and the Caribbean (ECLAC). Sustainable Development: Changing Production Patterns, Social Equity and the Environment. Casilla 179-D, Santiago, Chile. 1991.

Gachuk, David. "Harambee in Kenya: A Case for its Regulation." Occasional Paper No. 19, July 1982. Revised version of one of nine papers presented at the AID/Shambaugh Conference on Local Political Organization and Rural Development Policy in Less Developed Countries held at the University of Iowa, Iowa City, Iowa. September 24-26, 1981.

Gibson, J. Eugene & William J. Schrenk. "The Enterprise for the American Initiative: A Second Generation of Debt-for-Nature Exchanges — With an Overview of Other Recent Exchange Initiatives." Vol 25: The George Washington Journal of International Law and Economics. 1991.

Hanson, Gary. "Terms of Endowment." Published by AID's CDIE. 1990.

Hopkins, Bruce R. & Cynthia L. Moore. "Developing Philanthropy Internationally: Legal Issues for Policymakers to Consider in Formulating a Country's Law of Charity."

Hyden, Goran. "From Dispensing Political Patronage to Generating Social Capital: African Development in Transition." Paper presented to the ATLAS Seminar/Conference on "Governance in Africa" held in Dakar, Senegal, April 21-26, 1992, under the auspices of the African-American Institute.

Lee, Judith F. et al. Realizing Investment Objectives Through a Morgan Diversified Portfolio. Morgan Guaranty Trust Company report, prepared for the World Bank Second Trust Fund Workshop, July 31, 1992.

Lion, Donor M. "Endowments and Intermediary Institutions." Labat-Anderson, Inc. Paper in draft form prepared for the Private Sector Initiative for Africa, USAID. 1991.

Nair, Govindan et al. Madagascar, Financial Policies for Diversified Growth: Choices for a Market Economy. The World Bank. October 28, 1991.

Rigby, John T. Joan Goodin, Elaine Robbins, "Report to USAID/Ecuador: Health and Family Planning Project - 518-0084." New TransCentury Foundation. March 1991.

Simmons, Emmy. "Notes on Malagasy Banking Sector." U.S. Agency for International Development, Regional Economic Development Services Office for East and Southern Africa. September 1992.

Tourreilles, Francisco A. Establishing a Trust Fund. The Nature Conservancy. July 1992.

Weatherly, W. P. and Warnken, P. "Programming Agricultural and Environmental Endowments and Foundations in Africa: Lessons from Latin America." A report to the USAID Bureau for Africa. January 1994.

Weatherly, W. P. "Recommendations for Development of the Tanzania AIDS Orphan Trust." Report to USAID/Tanzania. March 1993.

Weatherly, W. P. "Guidelines for Planning and Programming Endowments and Endowed Foundations in Africa." Revised draft report to AID's Africa Bureau: January 1993.

Weatherly, W. P., Gibson, J. E., and Callahan, D. "Notes on 1 December 1992 Endowments Colloquium." A report to the Africa Bureau of AID. January 1993.

Weatherly, W. P., and Gibson, J. E. "Review and Addition to Guidelines for Endowments to Environmental NGOs in Africa." A report to the Africa Bureau of AID. November 1992.

Weatherly, W. P., and Gibson, J. E. "Report on the Foundation for the Environment of Madagascar." A report to USAID/Antananarivo. October 1992.

Weatherly, W. P. "Guidelines for the Africa Bureau of AID for Programming LocalCurrency Endowments." Draft report to AID's Africa Bureau: October 1991.

Weatherly, W. P. "A Proposal for the Establishment of MEENS or the Madagascar Endowment for the Environment, Nature, and Society." June 1991.

Weatherly, W. P. "Two Case Studies: The Puerto Rico Community Foundation, and the Philippine National Environmental Foundation." A report to the Global Environment Facility. The World Bank, Washington, D.C. March 1991.

Weatherly, W. P. "Creating a National Environmental Foundation in the Philippines." A proposal contained in the Natural Resource Management Program, USAID/Manila, the Philippines. June 1990.

Weatherly, W. P. "Beyond Debt for Nature Swaps: Opportunities and Strategies for Environmental Activities in Asia." A report to the Asian Development Bank, Manila, the Philippines. January 1990.

U.S. Agency for International Development
Bureau for Africa
Office of Sustainable Development
Productive Sector Growth and Environment Division
Room 2744 NS
Washington, D.C. 20523-0089